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CASE NO. 815

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In The

SUPREME COURT OF THE UNITED STATES

October Term, 1968

THE OHIO CASUALTY INSURANCE COMPANY,
Petitioner,

vs.

UNITED STATES OF AMERICA,
Respondent.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

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Petitioner prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Sixth Circuit dated September 9, 1968.

OPINIONS BELOW

The opinion of the district court filed on May 1, 1967, and of the court below filed on September 9, 1968, are not yet reported, either officially or unofficially, and for convenience are appended to this petition as Appendix I and II.

JURISDICTION

The date of the judgment sought to be reviewed and the date of its entry are September 9, 1968.

There was no order respecting a rehearing and there was no order granting an extension of time within which to petition for certiorari.

Jurisdiction of the federal courts is based upon Section 4 (c) of the Commodity Credit Corporation Charter Act, as amended (15 USC § 714 (c)) and upon title 28 USC § 1345 in that the United States brought this action as the real party in interest based upon a claim of the Commodity Credit Corporation, its wholly owned corporate agency and instrumentality.

The jurisdiction of this court is invoked under United States Code, title 28, Section 1254 (1).

QUESTIONS PRESENTED FOR REVIEW

I. What is the standard of conduct to be applied in judging a government agency's dealings with the public and whether the courts below applied such standard to the acts of the Commodity Credit Corporation which willfully failed to disclose to the Appellant bonding company that its principal had been the subject of an ambiguous "Shortage Committee" report.

II. Whether in this case, where the Appellant was not entitled to a jury trial, the Court of Appeals' mere holding that the District Court findings were not "clearly erroneous" constituted the improper standard of review?

III. Whether the application by the Court of Appeals of its vague and uncertain standard of duty of disclosure upon a government agency to inform a compensated surety of information which comes to the agency's attention which would tend to impugn the integrity of the surety's principal, if allowed to remain unrevealed, will effectively prohibit surety bond companies from issuing surety bonds,

at reasonable premiums, wherein the federal government is obligee?

STATEMENT OF THE CASE

This is a landmark case in that it involves immediately and directly the extent to which the government can willfully employ and create a "Credibility Gap" or "Fairness Gap" in dealing in non-defense matters with private citizens.

The Court of Appeals and District Court both read the "minutes" document, set out in its entirety in Appendix III, p. 28, and without any other testimony or explanation concluded:

(1) The document discloses no wrongdoing of Ross, the principal on the surety bond of Ohio Casualty;

(2) Therefore the government (CCC) may willfully conceal the document from an insurer who has been asked to bond Ross.

Petitioner says:

(1) The document is at best ambiguous and therefore the District Court is clearly in error when it concludes there is *no* evidence of wrongdoing — there is at least ambiguous evidence;

(2) The government especially may not willfully create a "fairness gap" or "credibility gap" by concealing such an ambiguous document from a potential insurer whose bond premium ($75 per year) presupposes no independent investigation.

The standard of "credibility" and fairness applied to the government by the Court of Appeals and District Court was less than that set forth in the Restatement of Security. The Restatement of Security, section 124, provides:

§ 124. NON-DISCLOSURE BY CREDITOR.

(1) Where *before the surety has undertaken his obligation* the creditor *knows facts unknown to the surety that materially increase the risk* beyond that which the creditor has reason to believe the surety intends to assume, and the creditor also has reason to believe that these facts are unknown to the surety *and has a reasonable opportunity to communicate them to the surety,* failure of the creditor to notify the surety of such facts is a defense to the surety.

(2) Where, *during the existence of the suretyship relation, the creditor discovers facts unknown to the surety* which would give the surety the privilege of terminating his obligation to the creditor as to liability for subsequent defaults, and the creditor has reason to believe these facts are unknown to the surety and has a reasonable opportunity to communicate them to the surety without a violation of a confidential duty, *the creditor has a duty to notify the surety,* and breach of this duty is a defense to the surety except in respect of his liability for defaults which have occurred before such disclosure should have been made. (Emphasis ours) American Law Institute, Restatement of Security, Section 124.

In contrast to this, the District Court said:

"A meeting of the Shortage Committee of the Department of Agriculture on June 14, 1960, concerning 2,628.57 bushels of corn valued at $2,997.84 was called to ascertain the location of certain warehouse receipts which apparently had been lost by Commodity Credit Corporation. The United States did not have knowledge of any actual shortages of grain on June 14, 1960 at the Ross Elevators, Inc. facilities. The United States did not have knowledge of any grain shortage in the Ross Elevators, Inc. storage facilities or knowledge of any default of Ross Elevators, Inc. under the Uniform Grain Storage Agreement prior to July 20, 1962." (Appendix III, p. 28)

This case involves a civil action brought by the United States on behalf of Commodity Credit Corporation (hereinafter referred to as CCC) to recover certain sums from The Ohio Casualty Insurance Company (hereinafter referred to as Ohio Casualty) under Ohio Casualty's Warehouseman's Bond No. 977055-7, executed July 18, 1960, in the penal sum of $15,000.00 and $4,000.00 rider thereto, executed February 22, 1962, by reason of alleged shortages in grain stored by CCC under the terms of a Uniform Grain Storage Agreement with Ross Elevators, Inc., the principal under the Ohio Casualty surety bond. The contention of Ohio Casualty at the trial of the matter was that the government had actual or imputed knowledge of real or potential shortages of grain or imputed knowledge of a default by Ross Elevators, Inc. prior to the execution by Ohio Casualty (at the request of CCC) of the surety bond in question. This information was not disclosed to Ohio Casualty, the proposed surety and, therefore, Ohio Casualty defended this action on the basis that the bond and rider thereafter executed by the surety was void ab initio.

At the trial of the matter Ohio Casualty also raised as an issue the affirmative duty upon the government, as obligee under a surety bond, to notify the proposed surety of all information which comes to the obligee's attention which would tend to impugn the integrity of the surety's principal. The Court of Appeals below failed to consider this issue raised to the effect that a government agency should be held to an even higher standard of disclosure than an individual under similar circumstances. Petitioner believes that the cursory disposition of this issue by the court below avoids the very fundamental issue of federal law involved in this case which has universal significance to the federal government in its basic dealings

with bonding companies and also to the standard of review to be followed by a Court of Appeals in such cases.

Under the terms of the bond in question Ohio Casualty, as surety, was contracting to bond the CCC, as obligee, against any losses it might sustain by reason of shortages in grain stored at Ross Elevators, Inc., the principal under the bond.

There is no question that on July 20, 1962, when load-out orders were issued by CCC to Ross Elevators, Inc., Ross failed to re-deliver certain grain and CCC sustained substantial shortages in the storage of grain at Ross Elevators. Petitioner at no time has sought to dispute the fact that grain shortages occurred at Ross Elevators, Inc. To the contrary Petitioner has consistently attempted to show that not only did grain shortages exist, but that shortages existed *prior* to the execution of the July 18, 1960 surety bond and that the government, as obligee under this bond, had information in its possession material to the risk Ohio Casualty was being asked to assume. This information related directly to prior defalcations of the proposed principal, Ross Elevators, yet the government, as obligee under the surety bond, did not disclose this material information to Ohio Casualty, the proposed surety.

The record is undisputed to the effect that a meeting of the Commodity Credit Corporation "Shortage Committee" was held on December 22, 1959 regarding shortages of grain stored at the Ross Elevator facilities. Again, on June 14, 1960, being a mere thirty-four days prior to the execution of the surety bond, the CCC called a further meeting of the Shortage Committee regarding Ross Elevator shortages. While the CCC contends there was no actual shortage, the reports are at best ambiguous and therefore cry out for disclosure to the surety rather than secretion by the government.

Ohio Casualty, as prospective surety for Ross Elevators, was not notified or in any way advised of either CCC Shortage Committee meeting regarding real or potential shortages of their prospective principal, nor given the ambiguous minutes report thereof.

Thereafter, on July 18, 1960, pursuant to the request of CCC, Ohio Casualty executed its surety bond in the amount of $15,000.00 with Ross Elevators, Inc., as principal and the CCC as obligee.

The surety bond contract form so executed was drawn by and insisted upon by CCC, the obligee. For the $15,000.00 bond coverage Ohio Casualty received a premium of $75.00 per year — not enough, of course, to warrant any affirmative investigation of its principal.

After July 18, 1960, when the $15,000.00 bond was issued, the CCC undertook periodic examinations and inspections of the amount of grain stored at Ross Elevator facilities.

Section 20 (b) (i) and (ii) of the Uniform Grain Storage Agreement drafted by CCC and executed by Ross Elevators, Inc. and CCC, which is the subject of the surety bond here in question, specifically requires the warehouseman to keep "daily position records" showing the total quantity of grain received and loaded out by him each day and the total quantity of grain remaining in the warehouse as of the close of each business day.[1]

---

[1] Section 20 (b) The warehouseman shall maintain current and complete records at all times with respect to all grain (including grain owned by him as well as other grain not subject to the terms of this agreement) which is stored in or handled through the warehouse. Such records shall include but not be limited to a daily position record showing:

(i) the total quantity of each kind and class of grain received and loaded out and the quantity of each kind of grain remaining in the warehouse as of the close of each business day and,

(ii) the warehouseman's total storage obligations for each kind and class of grain as of the close of each business day.

The evidence at the trial of this matter was undisputed that the storage facilities and quantity of grain stored at the Ross facilities were checked by CCC inspector, Edward L. Cassier, on March 15, 1961, July 21, 1961 and December 15, 1961. On each of these occasions the written report of the CCC examiner stated that Ross Elevators, Inc. *did not maintain* a satisfactory set of records reflecting its current storage liability and inventory and that *no* daily position sheets were maintained at all. Although this was a direct and continued breach of the express terms of Section 20 (b) (i) and (ii) of the Uniform Grain Storage Agreement no copy of any of these reports were ever sent to the bonding company, nor was Ohio Casualty contacted in any other manner to advise them of these facts known only to the CCC, the obligee under the bond. The surety was thus denied the opportunity to step in on behalf of the principal and take what action it deemed necessary to cure the breach by Ross of the terms of the Uniform Grain Storage Agreement.

Thereafter, on February 22, 1962, the CCC, as obligee under the bond here in question, requested Ohio Casualty to increase the penal sum of the bond from $15,000.00 to $19,000.00.

The CCC still did not advise Ohio Casualty of any of the information contained in their files relative to the failure of Ross to keep daily position sheets or of the meetings of the CCC Shortage Committee to consider shortages of grain at Ross facilities. In the absence of such information Ohio Casualty agreed to such an increase *although* the evidence at the trial of the matter was clear that had Ohio Casualty known of the facts known *only* to CCC, to the effect that Ross was not maintaining daily position sheets showing grain storage obligations, Ohio Casualty would definitely not have agreed to any increase.

At the trial of the matter, Mr. William R. Hedgecock,

Fidelity Surety Bond Supervisor for Ohio Casualty, as an expert in the field of suretyship bond underwriting testified that *the very fact* that the CCC Shortage Committee met on two separate occasions regarding its prospective principal and that the proposed principal had not been maintaining daily position sheets *would each be material* factors in the consideration of a surety in the issuance or continuance of a surety bond on such a principal. Specifically, Mr. Hedgecock testified that both of these factors go directly to the "integrity" of a principal which Hedgecock deemed to be a material underwriting condition precedent to the issuance and continuance of a suretyship bond. Mr. Hedgecock's expert opinion as to the materiality to a surety of these facts, not disclosed by CCC, in a surety's decision whether to issue or continue a bond was *unrebutted* and in no way controverted.

Even though this expert testimony as to the material nature of the undisclosed facts was unrebutted the District Court in its opinion entirely disregarded this highly relevant testimony. The Court of Appeals in its decision, dated September 9, 1968, also wholly omitted any consideration of, or even a reference to, this unrebutted and uncontroverted evidence.

By blindly following the outline of the facts as set forth in the findings of fact and conclusions of law set out by the District Court on May 1, 1967, Petitioner asserts that the Court of Appeals has failed to apply the standard of review required of it in such a case as is presented in this petition. The unavoidable result is an unreasonable and unworkable *absence* of a standard of duty of disclosure upon the government in such an important category of cases as is now before this honorable court.

ARGUMENT AMPLIFYING REASONS RELIED UPON FOR ALLOWANCE OF THE WRIT

The Court of Appeals for the Sixth Circuit has decided an important question of Federal law which has not been but should be settled by this Court.

Petitioner respectfully represents to this honorable court that if the decision of the District Court, as affirmed by the Court of Appeals, is allowed to stand it will result in substantial and continued future litigation between the United States government, as obligee on surety bonds, and numerous surety bonding companies, as surety on such bonds. Furthermore, Petitioner submits that the net effect of the decision of the Court of Appeals will effectively discourage surety bonding companies from issuing surety bonds in the future, at reasonable premiums, where the United States government is the obligee.

The real issue which the Court of Appeals totally avoided relates to the duty which the government, as obligee, has to a compensated surety to advise the surety of material facts known only to the obligee which would tend to impugn the integrity of the surety's principal.

The Court of Appeals apparently recognized the fact that the "Shortage Committee" of the CCC met on two separate occasions regarding real or potential shortages of grain stored at Ross facilities and that these meetings were held immediately *prior* to the CCC's request to Ohio Casualty to issue the surety bond here in question. Yet the Court of Appeals, in its decision, wholly misses the point sought to be raised by Petitioner in its appeal and, thus, in effect applies an unworkable standard of duty of disclosure to this type of surety bond case.

The Court of Appeals cites the annotation set forth at 8 ALR 1485, 1490, as a general statement of the duty of disclosure imposed upon an obligee of a bond where

the obligee has knowledge of material facts affecting the risk bonded, as follows:

> "To discharge the surety on the ground that the obligee has concealed or withheld from him material facts affecting the risk, there must be a duty on the part of the obligee to make disclosure, it being well settled that unless this duty arises under the circumstances of the particular case, the surety will not be released from his obligation by the mere fact that he did not have information which the obligee possessed, affecting the risk, and which would have probably prevented his signing the contract; in other words, there is nothing in the mere nature of the contract of suretyship itself which requires the obligee to disclose to the proposed surety all the material facts affecting the risk."

Also see, e.g. *Magee* v. *Manhattan L. Ins. Co.,* 92 U.S. 93, 23 L. Ed 699 (1876); 72 C.J.S., Principal and Surety, § 77.

While the foregoing quotation sets out the general duty imposed upon an obligee, the Court of Appeals in its decision wholly overlooks significant factors present in this case when determining whether such a duty of disclosure arose. The Court directed its attention to whether or not any actual shortages of grain were found at the two "Shortage Committee" meetings and totally avoided the material issue raised by the Shortage Committee meetings. Petitioner represents that the material issue to the surety was *the very fact that these Shortage Committee meetings took place* — not how many bushels of grain Ross may or may not have been determined to have been short at that time.

The unrebutted testimony of William Hedgecock, an expert in surety bond underwriting was that *the very fact that these meetings were held was material* to a proposed surety so as to call to the surety's attention the question

of the integrity of the proposed principal. In the opinion of the expert in surety bond underwriting the very fact that the meetings of the Shortage Committee took place would cause a bonding company not to have issued the bond. By looking back at these Shortage Committee meetings from some eight years later and making a simple determination that the Shortage Committee meetings, held in 1960, did not disclose to the government sufficient knowledge of defactions of the principal so as to impose *any* duty of disclosure is to apply, by hindsight, an unworkable and unreasonable standard of duty which totally avoids any relationship to the basic factors which a surety bonding company deemed relevant and material in its determination of whether or not the integrity of a proposed principal justified the issuance of a surety bond.

By applying such a strict standard of disclosure the Court of Appeals has set forth in this case a formidable barrier to any surety bonding company's issuance of a bond where the federal government is obligee. A bonding company would have to assume the risk of the government having undisclosed knowledge of material facts bearing upon the integrity of its proposed principal since there exists such a nebulous and uncertain duty of disclosure. Thus, because of the decision of the Court of Appeals in this case it may eventually be impossible for the government to procure, for a reasonable premium *any* surety bonds where the government is obligee.

Petitioner further suggests that the portion of the decision of the Court of Appeals finding an absence of duty of disclosure on the part of the government as to knowledge of the principal's *continuing breach* of the express terms of Section 20 of the Uniform Grain Storage Agreement constitutes an even more serious factor which might result in the cancellation, by surety bonding companies, of surety bonds wherein the government is obligee.

While the Court of Appeals recognized the undisputed fact that the principal was engaged in a continual breach of the express terms of the agreement which constituted the undulying basis for the bond by failing to keep the required daily storage records, such a breach was found by the Court *not* to be a "material default" under the grain storage agreement. As the sole support for this decision the Court cited 72 C.J.S. Principal and Surety Sec. 150, at 637-38:

> "(A) surety is not discharged from further liability generally, on failure of the obligee to notify him of his principal's default, *where the suretyship contract contains no stipulation that such notice shall be given,* . . . even where the bond requires notice, the surety is not discharged by a failure to give notice of *slight defaults, which are waived by the obligee;* or on mere suspicion of possible default; . . . or where the surety already has knowledge or is chargeable with knowledge of the default." (emphasis added)

Petitioner respectfully submits that this portion of the decision of the Court of Appeals again avoids the very facts of this case and, therefore, contributes to the application of an improper standard of duty of disclosure.

While it is true that "the suretyship contract contains no stipulation that such notice (of default) be given", it should be borne in mind that this suretyship agreement was *drawn by the government,* the obligee, and not by the surety. This is not a case of the construction of an insurance policy where ambiguities in the language are to be construed most strongly in favor of the insured and against the insurance company. On the contrary, this is question of the construction of a contract of *suretyship.* The decision of the Court of Appeals, if not reversed, would place upon a suretyship contract the same rules of construction as that applied to standard insurance contracts.

The law relating to the construction to be given *suretyship contracts* is generally set forth as follows:

> "If there is doubt or uncertainty as to the meaning, growing out of ambiguity of language, which makes construction necessary, the doubt will be resolved in his (surety's) favor." 50 Am Jur, Suretyship, Section 32

Also in support of the principle that a suretyship contract is to be construed in favor of the surety are: *St. Paul Fire & Marine Ins. Co.* v. *U. S.,* (CA 8 ND), 309 F2d 22; *Eistrat* v. *Massachusetts Bonding & Ins. Co.,* (CA 9 Cal.) 224 F2d 784.

Petitioner submits that not only should the language of the surety bond be construed *in favor of Ohio Casualty,* the surety, but it is also fundamental that doubtful language in a contract should be interpreted most strongly *against* the party who drew or prepared the contract. 17 Am Jur 2d, Contracts, Sec. 276; *Mouler* v. *American Life Ins. Co.,* 111 U.S. 335, 28 L. Ed 447, 4 S. Ct. 446. Here the surety contract was drawn by the government, the obligee, and should be construed *against* them.

Petitioner further submits that there were no "slight defaults . . . waived by the obligee" even suggested in the record of the trial of this matter. The testimony contained in the record is to the effect that in the opinion of an expert in surety bond underwriting *the very failure to keep such records* was a *material* default in the agreement, hence there could have been no "waiver" of *"slight"* defaults.

While the Court of Appeals did refer to the argument raised by Petitioner that a surety has the right to stand on the letter of his contract, and if, without his knowledge or consent, any material alteration or change, to his prejudice, is made in the contract, he is discharged (*Golden*

West Construction Company v. *U. S.*, 304 F2d 753 (CA, 1962); *Reliance Insurance Co. of Philadelphia, Pa.* v. *Colbert*, 365 F2d 530, (CADC, 1966)). The Court apparently did not give weight to this argument for the reason that the language of the Uniform Grain Storage Agreement (drawn by the obligee) contained an alleged "waiver" of notice of "all *duly authorized* modifications" to the agreement.

Petitioner respectfully submits that this construction given to the wording of the surety bond contract, drawn by and insisted upon by the *government*, was again an example of the confusion by the court of the rules of construction applied to *insurance* contracts and the rules of construction to be applied *suretyship* contracts. Furthermore, the record is devoid of evidence that these material modifications in the agreement were in any way "duly authorized" by the government, as obligee. To have knowledge of these material modifications and to permit them to continue to exist is not necessarily tantamount to "duly authorizing" the modifications. This material default could not be "waived" by the obligee without effectively unilaterally changing the basic contract of suretyship thus discharging the surety.

The Court of Appeals reinforces their stringent test to determine when the duty to disclose arises by suggesting that the surety should be chargeable with knowledge of the default of Ross in failing to keep the required records of grain storage. Petitioner asserts that this facet of the decision of the Court of Appeals, if allowed to remain unreversed, will, standing alone, force a drastic change in the premium schedules currently existing between the government and surety bonding companies. For the $15,000.00 bond involved in this matter, Ohio Casualty, as surety, received the nominal bond premium of approximately $75.00 per year. The application of a standard by

the Court of Appeals which would effectively charge a bonding company, receiving only a $75.00 per year premium, with the obligation of making its own independent investigations into the background of a proposed principal and to constantly check the records of such principal to uncover any defaults by the principal in the underlying agreement which is the basis of the suretyship is both unreasonable and unworkable.

Petitioner submits that any obligation placed upon a surety to make an independent inquiry as to the integrity and performance of its principal should be directly related to the amount of the premium received. Where the premium is nominal the surety, as a matter of basic economics, cannot expend substantial labor and time investigating and conducting continual checks on the conduct of its principal. Petitioner submits that the obligation of disclosure of facts coming into the obligee's knowledge in such cases is *greater* than in those instances where the bond premium is sufficient to justify the placing of the burden of an active investigation and inspection on the surety.

It is fundamental that a gratuitous surety is a favorite of the law and will be held to a lower standard of care that a compensated surety. 50 Am Jur, Suretyship, Section 32. While Ohio Casualty would not contend that it acted here as a gratuitous surety it is respectfully submitted that in view of the issuance of the surety bond for such a nominal premium, the application by the Court of Appeals of a severe and unreasonable standard of duty of disclosure, if allowed to remain unreversed, may result in the total abandonment by surety bonding companies of the field of surety bond underwriting where the government would stand as obligee.

Thus, the decision of the court below interpreting an important matter of law directly affecting and of great

and continuing importance to the federal government leaves the law in uncertainty, and the determination of this question by this Court will settle the point of law and remove the uncertainty as to this important question of law.

Wherefore, it is respectfully submitted that this Petition for writ of certiorari to review the judgment of the Court of Appeals for the Sixth Circuit should be granted.

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APPENDIX I

UNITED STATES DISTRICT COURT
Southern District of Ohio
Western Divison

CIVIL ACTION NO. 3212

UNITED STATES OF AMERICA,
Plaintiff,

vs.

THE OHIO CASUALTY INSURANCE COMPANY,
A CORPORATION,
Defendant.

FINDINGS OF FACT
CONCLUSIONS OF LAW
JUDGMENT

(Filed May 1, 1967)

This is a civil action authorized by the Attorney General of the United States based upon a claim of Commodity Credit Corporation. Defendant, The Ohio Casualty Insurance Company, is an Ohio corporation doing business in the State of Ohio. Ross Elevators, Inc. was an Ohio corporation, which entered into a Uniform Grain Storage Agreement with the Commodity Credit Corporation on June 30, 1960.

On September 27, 1962, the United States sued Ross Elevators, Inc. and The Ohio Casualty Insurance Company to recover all damages sustained by the United States arising under a uniform Grain Storage Agreement executed between Ross Elevators, Inc. and Commodity Credit Corporation. On June 13, 1963, a judgment of default was entered against Ross Elevators, Inc., in Civil Action No. 2790. Ross Elevators, Inc. by their default admitted that the allegations contained in the complaint were true. On December 18, 1964, The Ohio Casualty Insurance Company was dismissed as a party defendant.

On June 21, 1965 a deficiency judgment was awarded to the United States against Ross Elevators, Inc., in the sum of $65,275.89 arising from transactions between them under the Uniform Grain Storage Agreement dated June 30, 1960, as computed pursuant to the terms of said agreement in the regular course of business of the Commodity Credit Corporation.

On July 18, 1960, Ross Elevators, Inc., as principal and The Ohio Casualty Insurance Compa..y, as surety, executed a Warehouseman's Bond No. 977055-7 in the penal sum of $15,000. The bond provided that Ross Elevators, Inc., as principal, and The Ohio Casualty Insurance Company, as surety, are held and firmly bound, unto Commodity Credit Corporation and to any agency or person who may be injured by a breach of the Uniform Grain Storage Agreement dated June 30, 1960.

In December 1961, Ross Elevators, Inc. leased 15 bins from Commodity Credit Corporation and increased their storage capacity from 159,972 bushels to 206,184 bushels under the Uniform Grain Storage Agreement. On March 7, 1962, Ross Elevators, Inc. and The Ohio Casualty Insurance Company executed a rider to the Warehouseman's Bond No. 977055-7 increasing the penal sum of the bond

from $15,000 to $19,000 effective February 22, 1962 due to the increased storage capacity of Ross Elevators, Inc. On July 20, 1962, Commodity Credit Corporation was the holder of warehouse receipts issued by Ross Elevators, Inc. for 43,638.24 bushels of soybeans and 62,711.57 bushels of corn.

All of the grain stored by Ross Elevators, Inc. was stored on a commingled basis. There was no mutual agreement in writing, or verbal agreement confirmed in writing between Commodity Credit Corporation and Ross Elevators, Inc. that grain would be stored identity preserved. All grain stored at the Ross Elevators, Inc. storage facilities was not stored in sealed bins under supervision by a disinterested custodian. During the period 1957 through 1962, Commodity Credit Corporation paid Ross Elevators, Inc. the commingled rate of storage for soybeans and corn which was the highest rate of storage.

The Uniform Grain Storage Agreement in paragraph 11 (j) provides that the warehouseman shall be liable as an insurer and indemnify Commodity Credit Corporation for any failure to deliver grain meeting the requirements of their contract.

Commodity Credit Corporation issued "Shipping Instructions, Loading Order, Trust Order and Invoice" documents No. 31761090, 31761091, 31700092, 31700093, 31700094, 31700095, and 31700096 requiring the shipment of 43,638.24 bushels of soybeans and 62,711.57 bushels of corn. The lowest market price of soybeans at Union City, Ohio between March 1, 1962 and December 31, 1962 was $2.15275 per bushel. The lowest market price of Grade 2 yellow corn at Union City, Ohio between March 1, 1962 and December 31, 1962 was $1.02840 per bushel. The lowest market price of Grade 3 yellow corn at Union City, Ohio between March 1, 1962 and December 31, 1962 was $1.01840 per bushel.

During the period July 25, 1962 and October 18, 1962, Ross Elevators, Inc. failed to ship or otherwise redeliver to Commodity Credit Corporation 35,149.66 bushels of corn at $1.02840 per bushel and 2,471 bushels of corn at $1.01840 per bushel and overdelivered 2,585.54 bushels of corn at $1.02840 per bushel for a total amount of corn not delivered of 35,035.12 bushels valued at $36,005.41. Ross Elevators, Inc. failed to ship or otherwise redeliver to Commodity Credit Corporation 4,248.39 bushels of soybeans at $2.15275 per bushel for a total value of $9,145.72.

A meeting of the Shortage Committee of the Department of Agriculture on June 14, 1960, concerning 2,628.57 bushels of corn valued at $2,997.84 was called to ascertain the location of certain warehouse receipts which apparently had been lost by Commodity Credit Corporation. The United States did not have knowledge of any actual shortages of grain on June 14, 1960 at the Ross Elevators, Inc. facilities. The United States did not have knowledge of any grain shortage in the Ross Elevators, Inc. storage facilities or knowledge of any default of Ross Elevators, Inc. under the Uniform Grain Storage Agreement prior to July 20, 1962.

CONCLUSIONS OF LAW

The Court has jurisdiction of the parties and of the subject matter in this controversy. 15 U.S.C. Section 714 (b) (c).

Under the provisions of the Uniform Grain Storage Agreement, Ross Elevators, Inc. was an insurer of all of Commodity Credit Corporation's grain.

Ross Elevators, Inc. breached its Uniform Grain Storage Agreement with Commodity Credit Corporation by failing to redeliver 35,035.12 bushels of corn and 4,248.39 bushels of soybeans to Commodity Credit Corporation valued at $45,151.13.

The defendant, as surety, became liable for the principal sum of its bond in the amount of $19,000 when Ross Elevators, Inc. failed to redeliver to Commodity Credit Corporation, pursuant to the provisions of the Uniform Grain Storage Agreement, corn and soybeans valued at $45,151.13.

The plaintiff can recover interest at 6% on the principal sum of $19,000 from June 13, 1963, when the judgment of default was entered against Ross Elevators, Inc.

Where the bond contained no provision that the plaintiff give notice to the defendant of the principal's default, failure to give such notice does not discharge the surety.

JUDGMENT

Plaintiff shall recover the sum of $19,000 with interest at 6% from June 13, 1963.

. . . . . .

Chief Judge U. S. District Court

APPENDIX II

UNITED STATES COURT OF APPEALS
For The Sixth Circuit

No. 18035

UNITED STATES OF AMERICA,
Plaintiff-Appellee,

v.

THE OHIO CASUALTY INSURANCE CO.,
Defendant-Appellant.

Appeal from the U.S. District Court for the Southern District of Ohio.

Decided September 9, 1968

Before: O'SULLIVAN, PHILLIPS and EDWARDS, Circuit Judges.

O'SULLIVAN, Circuit Judge. On June 30, 1960, the Commodity Credit Corporation entered into a Uniform Grain Storage Agreement for the storage of agricultural commodities with Ross Elevator Company. The agreement required Ross to furnish a surety bond for the benefit of the CCC. Pursuant thereto Ross on July 21, 1960, obtained a $15,000 surety bond from the Ohio Casualty Insurance Company. On March 7, 1962, a rider was attached to the bond increasing its amount to $19,000 due to growth in Ross' storage capacity.

On July 20, 1962, a CCC inspector making a routine check of Ross' facilities and records discovered a large shortage of CCC commodities of a value in excess of the $19,000 surety bond. The CCC immediately removed its commodities and, having failed to obtain reimbursement from Ross for the shortage, commenced suit and obtained judgment against Ross for $65,275.89, which went unsatisfied. The CCC then sued appellant herein on its $19,000 surety obligation.

Appellant admits on this appeal, as it did in the District Court, that it is bound by the aforesaid judgment against its principal, Ross Elevator, if the bond in question is legally enforceable. As stated at page 6 of its brief:

> "As indicated above, Ohio Casualty does not dispute that the dollar amount of the loss claimed by CCC, exceeds the amount of the surety's obligation, but does dispute the legal validity and enforceability of the surety bond and rider."

It defends against liability under the bond on two bases: 1) that the CCC withheld material information regarding the integrity of Ross Elevators, known to the CCC at the time of the issuance of the bond; and 2) that the CCC learned on March 15, 1961, that Ross was not keeping "daily position sheets," but failed to disclose this to the surety. For the reasons which follow we reject these contentions and affirm the judgment of the District Court.

1. Nondisclosure Prior to Issuance of Bond.

The District Court made the following finding of fact:

> "A meeting of the Shortage Committee of the Department of Agriculture on June 14, 1960, concerning 2,628.57 bushels of corn valued at $2,997.84 was called to ascertain the location of certain warehouse re-

> ceipts which apparently had been lost by Commodity Credit Corporation. *The United States did not have knowledge of any actual shortages of grain on June 14, 1960, at the Ross Elevators, Inc. facilities.*"

It is not contended by appellant that said meeting (or an earlier one which apparently also had been held) disclosed any actual shortages of grain at Ross Elevators, Inc. Appellant argues, rather, that the CCC had a duty to disclose to the surety the bare fact that these meetings had taken place. The testimony of appellant's Fidelity Surety Bond Supervisor that such meetings would "indicate a lack of *integrity* or ability in storing grain," and that he would not have issued the bond had he known of the meetings, is said to compel the conclusion that the informatior was "material" and that a duty to disclose on the part of CCC was thereby created.

Appellant has quoted and cited in its brief to us cases inapposite to the factual situation here presented. These cases involve the failure of an employer, in obtaining a fidelity bond for his employee, to disclose to the surety the prior dishonesty or defalcations of the employee. Appellant quotes from an annotation at 4 A.L.R.3d 1197, 1199, the basic rule of law involved as follows:

> "It seems to be fairly well-settled that an affirmative misrepresentation or concealment by the obligee of a bond, of *prior defalcations* by the person to be bonded, will serve to excuse the surety from liability on the bond, since clearly such information is material to the risk to be assumed." (Emphasis supplied.)

CCC is said to have withheld information of "prior defalcations" of Ross Elevator. We cannot agree that such a conclusion follows from the aforementioned "shortages" meetings.

We think the applicable rule has been well put in 8 A.L.R. 1485, 1390, *Annotation: Obligee's concealment of facts or evasive answers as fraud against surety,* as follows:

> "To discharge the surety on the ground that the obligee has concealed or withheld from him material facts affecting the risk, there must be a duty on the part of the obligee to make disclosure, it being well settled that, unless this duty arises under the circumstances of the particular case, the surety will not be released from his obligation by the mere fact that he did not have information which the obligee possessed, affecting the risk, and which would have probably prevented his signing the contract; in other words, there is nothing in the mere nature of the contract of suretyship itself which requires the obligee to disclose to the proposed surety all the material facts affecting the risk."

See, e. g., Magee v. *Manhattan L. Ins. Co.,* 92 U.S. 93, 23 L.Ed. 699 (1876); 72 C.J.S. *Principal and Surety* § 77. We hold that the District Court committed no error of law nor were his findings clearly erroneous, F.R.Civ.P. 52(a), that in the circumstances of this case no duty devolved upon the CCC to make disclosure of the "Shortages" meetings.

2. Nondisclosure of Ross' Failure to Keep Daily Records.

Section 20 of the grain storage agreement between Ross and the CCC required Ross to keep "daily position sheets" of the inputs and outputs of agricultural commodities in its warehouse (other grain along with that of the government was stored on a comingled basis). On and after March 15, 1961, CCC inspectors noted on their inventory checks of Ross Elevators that said daily records were not being adequately kept. These checks, however,

revealed no actual shortages of commodities in the Ross facilities. Appellant contends that the acquiescence of the CCC in Ross' "default" amounted to a material alteration of the grain storage agreement without the knowledge and consent of the surety, and therefore discharged the surety. Even were this contention a correct statement of relevant law, it must in all events fail by virtue of the express language of the contract of suretyship itself, which provides: "Notice of * * * modifications [of the grain storage agreement] to the Surety being hereby waived * * *."

We think, furthermore, that the District Court was correct in concluding that the CCC did not have a duty to disclose to appellant Ross' failure to keep adequate records as a "material default" under the grain storage agreement. In this regard the discussion in 72 C.J.S. *Principal and Surety* § 150, at 637-38 is quite relevant:

> "[A] surety is not discharged from further liability generally, on failure of the obligee to notify him of his principal's default, where the suretyship contract contains no stipulation that such notice shall be given, * * * even where the bond requires notice, the surety is not discharged by a failure to give notice of slight defaults, which are waived by the obligee; or on mere suspicion of possible default; * * * or where the surety already has knowledge or is chargeable with knowledge of the default."

Judgment affirmed.

APPENDIX III

MINUTES OF CCC SHORTAGE COMMITTEE

(Dated June 17, 1960)

Messrs. Boberski, Pohlman, Kellert, Tyarks, Paskins, Norin and Shanesy

Marvin C. Smith

Ross Elevator, Union City, Indiana

A meeting of the Shortage Committee was held in my office on June 14, 1960, for the purpose of determining action to be taken in connection with a claim established in the amount of $2,997.84 covering 2,628.57 bushels of corn which was unaccounted for as farm stored deliveries. The following persons attended the meeting:

Marvin C. Smith, Chairman
J. M. Boberski
Edward Kellett
Thomas Walsh
E. R. Hokanson
Harold Shanesy
Albert Dohlman
William Hoffman
David Kushnir

The Shortage Committee met previously on December 22, 1959, on this case. The warehouseman visited this office and talked to Mr. Shanesy in regard to the matter. At the same time, he furnished us with copies of two negotiable warehouse receipts Nos. 54 and 97 covering the bushels of corn in question. These warehouse receipts were issued on 8/19/57 and 9/1/57. He indicated that the warehouse receipts had been lost by this office.

It was agreed that the following action should be taken:

(1) Claims Division to review all background information on the case.

(2) Claims Division to check with the County Office to determine if the original warehouse receipts are in file.

(3) If the Claims Division is unable to determine if the corn in question has been delivered to a bin site, shipped on a loading order or sold to them by CCC, they should accept the warehouse receipts and place them in inventory.

(4) Steps should be taken by the Claims Division to be certain that storage and handling charges are properly paid.

/s/ MARVIN C. SMITH

MCSmith/ajw
c. c. Director's Staff Copy